

Opinion: South Lake Tahoe justifies reallocation of \$7 million

To the community,

The following is a response to recent allegations of misappropriation of city/Redevelopment Agency funds in regards to actions that occurred approximately 10 years ago. The information presented comes from the public record, auditor's reports, evaluations conducted and discussions with staff that are currently or formerly employed by the city/Redevelopment Agency. The information is supplied to the best of our ability as most of the staff are no longer employed at the city or Redevelopment Agency.



At issue is the question of how the South Tahoe Redevelopment Agency developed a deficit of \$7,007,000 between the years 1999 and 2003. There is no evidence to suggest anyone "stole" the funds as recently alleged by Mr. Steve Kubby who has not presented any evidence to support such accusations.

Where did the deficit come from?

The accumulative deficit that occurred between the years of 1999-2003 were determined and found to be in the following line items:

Revenue reductions:

- \$500,000 late start at Park Avenue (less revenue than budgeted)
- \$371,076 in reduced property values of the Embassy Suites

- \$1,200,000 administrative costs advanced by the City

Excess expenditures:

- \$1,184,053 overhead charges the city “charged” the agency as described below (charging the agency was not anticipated at the time the budget was prepared and resulted in the budgets showing a deficit).
- \$1,800,000 excess expenses to acquire the Transit Center which were not known at the time the grant funds were received
- \$1,100,000 legal expenses related to acquiring property
- \$476,000 road construction costs higher than budgeted
- \$333,000 relocation costs higher than budgeted
- \$42,871 miscellaneous costs higher than budgeted

What caused the deficit?

As has been said in the past in the public record, the amount and causes of the deficit are not uncommon when projects are in the midst of getting built, when revenues come in less than anticipated and when project expenses are higher than budgeted. In this case, the developer was also going through bankruptcy, which contributed to the outcome. How the deficit occurred has been reviewed by a multitude of professionals and citizens, from the grand jury to lawyers, CPAs, auditors and councilmembers. No evidence of criminal or illegal conduct has been determined by appropriate authorities who reviewed the situation. The oversights or errors that were made can be debated and judged in retrospect, but the most important action is to reflect on them and make the necessary corrections to avoid similar situations in the future. Under new procedures in place today, the City Council would have been presented with a decision whether or not to continue to support and fund the projects before the actions taken to do

so were implemented, which did not occur in every instance between 1999 and 2003.

The grand jury looked into the financial matter of the deficit for two years, independent auditors have reviewed the records, contracts and expenditures and the \$7,007,000 deficit is accounted for as described above. The issue was discussed with the City Council at a public meeting in 2003 and a detailed accounting was presented to the City Council in a staff report for the March 16, 2004, meeting. At that same meeting a loan agreement between the city and agency was approved to create the process for repaying the city from Redevelopment Agency proceeds. To date, the agency has repaid \$4,000,000 to the city's general fund. The deficit issue, discussion of the oversights that occurred, along with proposed corrective actions have come before the City Council and the public many times in the years since the deficit was realized.

Most, if not all the errors or oversights that led to the deficit, were identified by the El Dorado Grand Jury in its review of the actions and which have been previously reported. Those of most significance include the following:

- Inadequate financial policies. In 2005, the City Council adopted a comprehensive set of financial policies to prevent the kind of errors that led to the deficit. Prior to 2005, the city did not have sufficient financial policies. While the use of the funds may not have been improper or outside the scope of the city manager's position and decision-making authority, the City Council upon learning of the deficit realized part of the problem was a lack of strict financial controls that would keep City Council more informed and provide them the opportunity to make the financial and policy decisions on matters of importance to the community and on significant projects. The adoption of the financial policies has led to significantly improved public and City Council involvement with respect to all levels of financial management and reporting.

- Lack of transparency with City Council. Some of the deficit was first reported in the 2001 and 2002 auditor's evaluation reports. Those auditor's reports were provided to the City Council, but not appropriately highlighted. The growing deficit should have been more directly brought to City Council's attention as soon as it was reported.
- Charging the Redevelopment Agency for "admin costs" when the agency didn't have funds. The City had a practice and cost allocation recovery policy to charge the Redevelopment Agency for the city's expenses it incurred to develop projects on behalf of the agency. This practice itself is appropriate to recover costs. However, it was known at the time that the agency didn't have any additional funds outside of the funds it was going to need to build the project(s) yet, the city billed the agency for those costs, which contributed over a million dollars to the deficit, the portion of which is literally "on paper." While it is proper for the city to recover costs it incurred, the process of billing the agency contributed (somewhat falsely) to the eventual total deficit.
- Poor communication. Inadequate communication between several city managers between 1999–2003, redevelopment project managers and Redevelopment Agency board of directors (City Council) appears to have contributed to the overall situation.

In retrospect, the errors or oversights that led to the deficit were not caused by a single person or single instance. The procedural issues that caused the deficit were understood upon reflection and examination after the projects were done, which provided the opportunity to improve. Looking back one can conclude, as the grand jury did when presented with all of the facts and information that the lack of financial management and policies, inadequate financial staffing at the senior management level, organizational culture and lack of transparency all contributed to the \$7,007,000 deficit.

New procedures in place

What is most important is to learn from our mistakes. To date the city has completely retooled its financial practices and continues to do so. These changes include:

- Comprehensive financial policies adopted by City Council in 2005 – these policies strengthened financial and management controls. A deficit of any amount is no longer possible without prior City Council authorization. New purchasing and grant management

policies have also been put in place since 2005. All of these policies place financial management controls over the city's finances, require multiple reviews of expenditures and provide for better accounting and public reporting.

- New budgeting and financial reporting – each year the budget process and documents have been improved resulting in recognition from the Government Finance Officers' Association for meeting the national standards for budgeting and financial reporting.

- Re-established the position of finance director to oversee and review expenditures. The position has authority to inquire of staff regarding budget expenses and ensure appropriate tracking procedures are in place to notify senior staff and City Council if and when budget concerns are realized.

- The hiring of new auditors through a competitive process in accordance with the recommended best practices of the GFOA.

- Updated purchasing policies limiting the authority of the city manager to sign contracts over \$30,000.

- Established a general fund reserve policy requirement to set aside 25 percent of the general fund operating expenses, which is currently fully funded. This is a remarkable turnaround from 2003 when the city's reserve fund was zero! This outcome is commendable as recently reported in the Sacramento Bee, "Dry Times for Many Rainy Day funds" (May 29, 2011) the city

of South Lake Tahoe has been identified as the second best among local governments in the region for the amount of reserve funds as a percentage of its general funds.

In 2010-11, the city's trend toward improved policies continued with:

- Hiring a new city manager tasked with improving the organizational culture, developing strategic plans and developing a five-year financial plan.
- Changing the process of preparing staff reports for City Council to include a review by the Finance and Legal departments to ensure appropriate funds have been budgeted and legal requirements are met.
- Appointing of a Fiscal Sustainability Committee comprised of members of the public at-large with business and financial backgrounds and expertise to review the city's finances and provide opportunity for unique perspectives.
- Adopting the Five-Year Financial Plan in March 2011 to reduce expenses and focus on financial priorities.
- Adopting a Strategic Plan to keep fiscal sustainability as a top priority of the city. Letter to community.
- Establishing new communication practices and improved responsiveness to concerns and questions raised by the public or employees.
- Creating accountability between city manager and City Council through a truly open door policy at the highest level of the organization to receive information, ideas and complaints.

City employees are encouraged to directly communicate with any member of senior staff, the public or city councilmembers.

Looking toward the future

The city continues to focus on improving its efforts to provide information to the public, senior management and to City Council. Errors or oversights will still happen, they always will in any organization. An ongoing review of financial policies, input from staff, City Council and citizenry along with improved accountability to the public for the city's performance will help to minimize errors. We appreciate the opportunity to respond about the events that occurred between 1999 and 2003 and hope this review helps to fill in any gaps that may have been missing.

We are now moving forward toward an improved, better prepared and focused city government.

We have committed to the citizenry and City Council to focus on the strategic priorities, which include improving the infrastructure and built environment, responding to public inquiries, involving the citizenry, focusing on our fiscal sustainability, bringing much needed jobs to the community and addressing issues of concern efficiently.

The citizenry can and should expect what the city has promised to deliver including:

- Performance measures for each strategic priority to allow rapid responses to changing conditions.
- Quarterly progress reports on our efforts to achieve stated goals.
- A new, improved user-friendly budget document and process involving a wide variety of input from citizens, City Council and city staff at all levels.
- Improved customer service and community relations providing opportunity for public input, debate and dialogue on the issues and routine feedback.
- A focus on improving the built environment so it will

correspond to the beauty of the natural environment.

- Better partnerships and responsiveness to local agencies and special interest groups to bring more projects to completion.
- And many others.

We welcome any suggestions or comments on any item of interest and at any time.

Nancy Kerry, South Lake Tahoe public affairs and communications manager